Report

of the

Examination of

Newark Mutual Insurance Company

Beloit, Wisconsin

As of December 31, 2002

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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November 7, 2003

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2002, of the affairs and financial condition of:

NEWARK MUTUAL INSURANCE COMPANY
BELOIT, WISCONSIN

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The last examination of this company was made in 1999 as of December 31, 1998. The current examination covered the intervening time period ending December 31, 2002, and included a review of such subsequent transactions deemed essential to complete this examination.

The “Summary of Examination Results” contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on March 16, 1875, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Newark Mutual Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation and no amendments to the bylaws.

The company is currently licensed to write property, including windstorm and hail, and non-property insurance. The company is currently licensed to write business in the following counties:

Dane	Green
Lafayette	Racine
Rock	Walworth

A review was made of the policy and application forms currently used by the company. The company issues an approved policy with or without endorsements for terms of one year with premiums payable on the advance premium basis. The company also charges a policy fee based on annual premium of the policy, fees are $20.00, $30.00, or $40.00 depending on the amount of the annual premium.

Business of the company is acquired through 37 agents, two of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	**Compensation**
Farm, Farmowners, Mobile Home	10 %
Homeowners, Residential, Commercial Public	15%

Agents do not have authority to adjust losses. Losses are adjusted by an independent adjuster hired by the company. The adjuster receives $12,000 per year for 110 losses to be adjusted, and is paid $100 per loss in excess of the 110 losses.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of nine members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Richard Hatlen*	Retired	Evansville, Wisconsin	2004
John Perkins	Purchasing Agent	Janesville, Wisconsin	2005
Paul Greenberg	Retired	Beloit, Wisconsin	2005
Neal Torkelson	Manager	Beloit, Wisconsin	2005
Karen A. Johnson*	Manager	Milton, Wisconsin	2006
Nancy Ladwig	Retired	Beloit, Wisconsin	2006
Robert Wildermuth	Farmer	Clinton, Wisconsin	2006
LaVerne Hays	Farmer	Orfordville, Wisconsin	2004
Vacant			2004

Directors who are also agents are identified with an asterisk. See the section of this report captioned Corporate Records regarding vacant directorship.

Members of the board currently receive $50.00 for each meeting attended and $.36 per mile for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified. Officers serving at the present time are as follows:

Name	Office	2002 Salary
Robert Wildermuth	President	$550
Neal Torkelson	Vice-President	$200
Karen A. Johnson	Secretary, Treasurer, Manager	$48,468

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee
Robert Wildermuth, Chair
Neal Torkelson
Karen A. Johnson
Richard Hatlen
John Perkins
Paul Greenberg
Nancy Ladwig
LaVerne Hays

Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2002	$260,561	1,210	$46,429	$528,347	$230,577
2001	271,417	1,087	(13,530)	509,569	251,570
2000	240,144	1,047	(105,375)	516,549	281,911
1999	144,341	1,031	(47,560)	472,366	325,418
1998	158,534	1,089	(81,177)	581,560	372,890

The ratios of gross and net premiums written to surplus as regards policyholders during the past five years were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Net	Writings Ratios Gross	NPW / GPW
2002	$589,126	$289,143	$230,577	125%	256%	49.1%
2001	522,559	284,057	251,570	113	208	54.4
2000	496,843	310,152	281,911	110	176	62.4
1999	450,726	105,296	325,418	32	139	23.4
1998	497,152	155,728	372,890	42	133	31.3

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Composite Ratio
2002	$ 84,238	$149,790	$260,561	32	52	84
2001	161,285	138,842	271,417	59	49	108
2000	222,478	142,131	240,144	93	46	139
1999	102,501	109,561	144,341	71	104	175
1998	127,874	124,171	158,534	81	80	161

The company has suffered net losses over three of the past four years. In 2000, the company had storms hit three different areas which caused the bad results for that year. In 2001, one area was severely hit again. In 2002, the company earned a profit, the first since 1996, however surplus decreased because of the decrease in the value of Wisconsin Reinsurance Corporation stock. Policies have grown to 1,210. At $230,577, reported surplus is barely above the minimum requirement of $200,000. The company’s composite ratio has been over 100% except for the current year’s 84%. This is due mainly to the high expense ratio of the company.

The high expense ratio is due in part to the company ceding a large percentage of its written premiums for reinsurance. Reinsurance rates are high due to prior losses paid by the reinsurer. In 1998 and 1999, the company retained only 31% and 23%, respectively, of premiums written, which resulted in expense ratios of 80% and 104%, respectively. Reinsurance contracts were revised in 2000, so the company retained greater risk exposure but reduced ceded premiums. This change allowed the company to reduce its expense ratio to the 46-52% range in the past three years. However, it will be difficult for the company to earn profits in an average loss year with an expense ratio in this range. The company needs to review its business plan to identify ways to reduce expenses.

The company has earned negative investment income in recent years, due to a combination of low market interest rates, few invested assets that produce a cash return, and expenses allocated to investment income ($11,526 in 2002) exceeded cash received from investments ($3,456 in 2002). About 41% of assets, or 93% of surplus, is invested in Wisconsin Reinsurance Corporation common stock, which does not pay dividends.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2003
Termination provisions:	Any January 1, with 90 days advance notice

The coverage's provided under this treaty are summarized as follows:

1.	Type of contract:	Class A – Liability 100% Quota Share
	Lines reinsured:	Liability
	Company's retention:	None
	Coverage:	100% of each and every liability loss $1,000,000 per occurrence, single or combined for bodily injury and property damage. $1,000,000 split limits, in any combination of bodily injury and property damage $5,000 medical payments per person, $25,000 per accident
	Reinsurance premium:	100% of the premium
	Ceding commission:	15% ceding commission
2.	Type of contract:	Class B - First Surplus
	Lines reinsured:	All property losses
	Company's retention:	Retained pro-rata portion of each risk
	Coverage:	When the company's net retention is $200,000 or more in respect to a risk, the company may cede on a pro rata basis, and the reinsurer shall be obligated to accept up to $800,000. When the company's net retention is $200,000 or less in respect to a risk, the company may cede on a pro rata basis, and the reinsurer shall be obligated to accept up to 50% of such risk.
	Reinsurance premium:	Pro rata portion of all premiums, fess and assessments

	Ceding commission:	15% standard sliding scale Minimum Commission: 15% Maximum Commission: 35%
3.	Type of contract:	Class C1 – First Layer Excess of Loss
	Lines reinsured:	All property business written by the company
	Company's retention:	$30,000 per loss occurrence
	Coverage:	100 % of each loss including loss adjusting expenses over the retention up to $70,000
	Reinsurance premium:	14.49% of net premiums written with a minimum premium of $49,000
4.	Type of contract:	Class C2 – Second Layer Excess of Loss
	Lines reinsured:	All property business written by the company
	Company's retention:	$100,000 per loss occurrence
	Coverage:	100% of loss and loss adjusting expenses in excess of $100,000 retention up to $100,000
	Reinsurance premium:	1.5% of net premiums written with a minimum premium of $5,000
5.	Type of contract:	Class D/E – Aggregate Stop Loss
	Lines reinsured:	All business written by the company
	Company's retention:	75% of the company’s net premiums written, minimum retention of $254,000
	Coverage:	100% of aggregate net losses in excess of retention
	Reinsurance premium:	8.3% of premiums written, with a minimum premium of $28,000

III. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2002, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Newark Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2002

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in company's office	$ 150	$	$	$ 150
Cash deposited in checking account	62,834			62,834
Cash deposited at interest	53,492			53,492
Bonds (at amortized cost)	361			361
Stocks or mutual fund investments (at market)	304,279			304,279
Real estate	9,951			9,951
Premiums and agents' balances and installments:				
In course of collection	7,268		451	6,817
Deferred and not yet due	84,684			84,684
Reinsurance recoverable on paid losses and lae	5,104			5,104
Electronic data processing equipment	675			675
Totals	$528,798	$ 0	$451	$528,347

Newark Mutual Insurance Company
Statement of Assets and Liabilities (cont.)
As of December 31, 2002

Liabilities and Surplus

Net unpaid losses	$16,500
Unpaid loss adjustment expenses	600
Commissions payable	11,100
Fire department dues payable	227
Unearned premiums	198,982
Reinsurance payable	68,629
Amounts withheld for the account of others	1,365
Payroll taxes payable (employer's portion)	50
Other liabilities:	
Expense related:	
Accounts payable	317
Total Liabilities	$297,770
Policyholders' surplus	230,577
Total Liabilities and Surplus	$528,347

Newark Mutual Insurance Company
Statement of Operations
For the Year 2002

Net premiums and assessments earned		$260,561
Deduct:		
Net losses incurred	$ 70,556	
Net loss adjustment expenses incurred	13,682	
Other underwriting expenses incurred	149,790	
Total losses and expenses incurred		234,028
Net underwriting gain (loss)		26,533
Net investment income:		
Net investment income earned		(8,070)
Other income:		
Fees		27,966
Net income (loss) before policyholder dividends and before federal income taxes		46,429
Net income (loss) before federal income taxes		46,429
Net Income (Loss)		$ 46,429

Newark Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2002

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2002	**2001**	**2000**	**1999**	**1998**
Surplus, beginning of year	$251,570	$281,911	$325,418	$372,890	$379,788
Net income	46,429	-13,530	-105,375	-47,560	-81,177
Net unrealized capital gains or (losses)	-68,199	-18,952	59,622	-2,158	71,533
Change in non-admitted assets	777	2,141	2,246	2,246	2,746
Surplus, end of year	$230,577	$251,570	$281,911	$325,418	$372,890

Reconciliation of Policyholders' Surplus

A reconciliation of the policyholders' surplus as reported by the company in its filed annual statement and as determined by the examination is detailed in the following schedule:

Policyholders' surplus per December 31, 2002, annual statement			$230,577
Item	**Increase**	**Decrease**	
Accrued Vacation Pay		$1,690	
Accrued Salaries		430	
Total		$2,120	
Decrease to Surplus per Examination			2,120
Policyholders' Surplus per Examination			$228,457

Examination Reclassifications

	Debit	Credit
Deferred Premium		$ 2,983
Unearned Premiums	$17,750	
Advance Premiums		14,767
Total reclassifications	$17,750	$17,750

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Corporate Records – It is recommended that the company document the number of policyholders present at each annual meeting so that it may be determined that a quorum was present.

   Action— Compliance.

2. Corporate Records – It is recommended that the company discuss and review the rent for TMA Agency on an annual basis as stated in the lease agreement.

   Action— Compliance.

3. Corporate Records – It is recommended that the board directors who have a material interest in an issue be excluded from the voting process and that this be noted in the meeting minutes, pursuant to s. 612.18, Wis. Stat., and s. 611.60 (2), Wis. Stat.

   Action— Compliance.

4. Corporate Records – It is recommended that the company adhere to its Articles of Incorporation as they relate to the replacement of a director during the elected term.

   Action— Noncompliance. See Corporate Records section of this report.

5. TMA Agency – It is recommended that the company develop proposed agreements for the transactions between the affiliates that comply with s. 611.61, Wis. Stat., and in accordance with s. 617.21, Wis. Stat., and s. Ins 40.04 (2), Wis. Adm. Code, submit these agreements to the commissioner, within 60 days after the adoption of this report.

   Action— Noncompliance. See the Holding Company section of this report.

6. TMA Agency - It is recommended that the company file holding company reports annually in accordance with s. Ins 40.03, Wis. Adm. Code.

   Action— Noncompliance. See the Holding Company section of this report.

7. Underwriting – It is recommended that the company update its written underwriting guidelines as these guidelines are changed by the board of directors.

   Action— Compliance.

8. Underwriting – It is suggested that the company have an individual or committee independent of the agent issuing the policy inspect a sampling of new and renewal policies.

   Action— Compliance.

9. EDP Environment – It is recommended that the company establish procedures to limit access to its computer.

   Action— Compliance.

10. Disaster Recovery Plan – It is recommended that the company develop a disaster recovery plan.

    Action— Compliance.

11. Cash and Invested Cash - It is recommended that the company prepares and retains a duplicate deposit ticket for each deposit.

    Action— Compliance.

12. Unpaid Losses – It is recommended that the company more accurately complete its loss register.

    Action— Compliance.

13. Unpaid Losses – It is recommended that the company adopt procedures for timely settlement of claims, in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.

    Action— Compliance.

14. Unpaid Loss Adjustment Expense – It is recommended that the company include an estimate for loss adjusting expense in its loss register in order to provide a more accurate estimate of the unpaid loss adjusting expense.

    Action— Compliance.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

The company has been operating with only eight directors for over two years. The articles of incorporation call for nine directors. The articles of incorporation also state the board may replace a director until the next annual meeting. The company has not replaced one director for over two years. In 1999, the company did replace directors, but did not have them elected at the next annual meeting. It is again recommended that the company replace directors according to its articles of incorporation and by-laws.

It was noted during the review of minutes that a director has missed six meetings in a row in the past year and during the period 1999-2000 another director missed 6 meetings in a row before resigning. The board should be made up of directors that can spend the time necessary to manage the company. It is recommended that directors be required to attend meetings regularly and, if any director cannot fulfill the obligation of regularly serving on the board, the company should consider replacing the individual with a person who is able to attend meetings regularly.

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with apparent conflicts being noted. One director notes being an agent and the other notes TMA Agency, Inc. See additional comments in the Holding Company section of this report regarding TMA Agency, Inc.

Holding Company

In 1989, the company sold the stock of TMA Agency, Inc., to two employees and four agents. Since the sale, agents who purchased TMA Agency, Inc. have retired or sold their interest in the agency. TMA Agency, Inc., is now owned by two key company employees, one of whom is a director of the company. TMA Agency, Inc., accounted for 48% of the premium in force in 2002, approximately $282,300. This percentage has stayed somewhat stable the past few years.

The company filed an agreement with this office showing that the annual rent to the agency would be $1,000 per year. The agreement also notes that the employees may conduct agency business during normal business hours, the agency will reimburse the company for long distance telephone calls not relating to the company's business and the agency will provide its own supplies. The company amended the agreement in 2002, effective January 2003, changing the rent to $1,100 per year, but did not file the change with this office. The agency also has the company's standard agency agreement with the company.

TMA Agency, Inc., and Newark Mutual Insurance Company are affiliates as defined by s. 600.03 (1), Wis. Stat. The companies are managed by the same group of people. The owners of TMA Agency, Inc., are the two key employees of Newark Mutual Insurance Company.

The prior examination had two recommendations regarding filing of agreements and holding company filings. The company has not filed Forms B, C or D during the examination period. It is again recommended that the company file with this office, agreements for transactions between affiliates pursuant to s. Ins 40.04 (2), Wis. Adm. Code. It is again recommended that the company annually file holding company reports in accordance with s. Ins 40.03, Wis. Adm. Code.

The company has a high expense ratio, and surplus has declined 45% from $418,660 at 1996 to $230,577 at 2002. The company pays its two key employees a full-time salary, and allows them to work on TMA Agency business during work hours. The company also pays TMA Agency the same commission rates as all other agents. It is suggested that the company re-evaluate its practice of paying its two key employees a salary and also paying TMA Agency the same commission rate as its other agents, in light of the company's diminished surplus and high expense ratio. It is also recommended that the company file an updated business plan with this office 30 days after the adoption of this report.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity bond	$100,000
Workers Compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	100,000
Each disease	100,000
Policy limit	500,000
Property - Building	93,600
- Personal	40,000
Liability - Professional	
Each Claim	1,000,000
Limit	1,000,000
- Directors and Officers	
Each Claim	1,000,000
Limit	1,000,000
For above liability combined limit	1,000,000

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. A sampling of new applications and of renewal business is inspected by an independent inspector. The inspector is paid $6,500 annually for inspections and is also the adjuster for the company.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2002.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's Electronic Data Processing environment. Access to the computers is limited to people authorized to use the computers.

Company personnel back up the computers daily and the backed-up data is kept off-site.

A manual which describes how to use the company's software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Disaster Recovery Plan

A disaster recovery plan identifies steps to be performed in case the company loses a key employee, is not able to access its computer, information on its computer was lost, or the office building was destroyed, to name a few contingencies. The company has developed a disaster recovery plan. The company's disaster recovery plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutuals allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$597,770
2.	Liabilities plus 33% of gross premiums written	492,182
3.	Liabilities plus 50% of net premiums written	442,342
4.	Amount required (greater of 1, 2, or 3)	597,770

5.	Amount of Type 1 investments as of 12/31/2002	184,615
6.	Excess or (deficiency)	($413,155)

The company does not have sufficient Type 1 investments.

The company has approval to hold Wisconsin Reinsurance Corporation (WRC) preferred and common stocks, NAMICO common stock and home office real estate. The company is in compliance with the investment rules, with the exception of a small bond which was purchased before the rule change; this bond matures in 2006 and is an immaterial amount.

ASSETS

Cash and Invested Cash **$116,476**

The above asset is comprised of the following types of cash items:

Cash in company's office	$ 150
Cash deposited in banks-checking accounts	62,834
Cash deposited in banks at interest	53,492
Total	$116,476

Cash in the company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in one bank. Verification of checking account balances was made by obtaining copies of the bank statement and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of two deposits in two depositories. Deposits were verified by viewing statements with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2002 totaled $448 and was verified to company cash records. Rates of interest earned on cash deposits ranged from .650% to .995%. There was no accrued interest on cash deposits at year-end.

The company had signature stamps for two directors. They were not used to sign checks but the company did not keep them secure, they were kept on a desk by a fax machine. There is a potential for their use on checks and therefore the following recommendation is being made. It is recommended that the company keep signature stamps in a secure place, such as the company safe.

Book Value of Bonds **$361**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2002. Bonds owned by the company are located in company’s fire proof safe.

Bonds were physically inspected by the examiners. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was not in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. The bond was purchased before the new rule, it will mature in 2006 and the amount is immaterial so no recommendation or adjustment will be made.

Interest received during 2002 on bonds amounted to $40 and was traced to cash receipts records. There was no accrued interest at December 31, 2002.

Stocks and Mutual Fund Investments $304,279

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2002. Stocks owned by the company are located in the company's fire proof safe.

Stock certificates were physically examined by the examiners. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2002 on stocks and mutual funds amounted to $1,968 and were traced to cash receipts records. There were no accrued dividends at December 31, 2002.

Book Value of Real Estate $9,951

The above amount represents the company's investment in real estate as of December 31, 2002. The company's real estate holdings consisted of the company office.

The required documents supporting the validity of this investment were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight line method.

Agents' Balances or Uncollected Premiums **$88,518**

The above ledger asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of individual agent's accounts verified the accuracy of this asset. The amount reported by the company was reduced by $2,983 for policyholder payments received prior to year-end that were still included in deferred premiums; this was part of a reclassification. See the comments in the Advance Premium account for more information.

Reinsurance Recoverable on Paid Losses **$5,104**

The above asset represents recoveries due to the company from reinsurance on losses which were paid on or prior to December 31, 2002. A review of year-end accountings with the reinsurer and subsequent receipt verified the above asset.

Electronic Data Processing Equipment **$675**

This asset consists of $675 of computer equipment owned by the company at December 31, 2002. A review of the depreciation schedule was used to verify this asset.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$16,500**

This liability represents losses incurred on or prior to December 31, 2002, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule. Differences are reflected in the section of this report captioned "Reconciliation of Policyholders' Surplus."

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	$73,124	$69,186	$3,938
Less: Reinsurance recoverable on unpaid losses	56,623	54,995	1,628
Net Unpaid Losses	$16,501	$14,191	$2,310

The examiners developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2002. To the actual paid loss figures was added an estimated amount for those 2002 and prior losses remaining unpaid at the examination date, if any. The above difference of $2,310 was not adjusted since IBNR claims may still be outstanding and it is conservative.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

Unpaid Loss Adjustment Expenses **$600**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2002, but remained unpaid as of year-end. The methodology used by the company in establishing this liability is to review outstanding claims and estimate the amount of adjusting expenses left to be paid. The company uses $100 per claim.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Unearned Premiums **$181,232**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology. The company included advance premiums and fees in their calculation of unearned premium. A reclassification entry was made debiting unearned premiums and crediting advance premiums in the amount of $17,750.

Advance Premiums **$14,767**

Advance premiums are payments received by the company prior to the policy renewal date. The company included advance premiums and fees in their calculation of unearned premium reserve. A reclassification entry was made debiting unearned premiums and crediting advance premiums in the amount of $17,750. In addition, there was $2,983 of Advance premiums that was still reported in the deferred premiums account. There was a reclass entry made for this also.

Reinsurance Payable **$68,629**

This liability consists of amounts due to the company's reinsurer at December 31, 2002, relating to transactions which occurred on or prior to that date.

Deferred Premium Payable	$ 15,433
2002 Adjusted Billing	
Class A	20,369
Class A Commission	(3,055)
Class C-1	8,000
Class C-2	900
Class D/E	6,700
December 2002 Billing	
Class A	7,750

Class A Commission	(1,163)
Class C-1	3,150
Class C-2	400
Class D/E	2,600
First Surplus	8,876
First Surplus Commission	(1,331)
Total	$68,629

Subsequent cash disbursements and or reinsurance accountings verified the amount of this liability.

Fire Department Dues Payable **$227**

This liability represents the fire department dues payable at December 31, 2002.

The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Commissions Payable **$11,100**

This liability represents commissions payable on deferred premiums. Examiners performed an analytical review to verify accuracy of calculation. Examiners also tested payments for accuracy.

Amounts Withheld for the Account of Others **$1,365**

This liability represents employee payroll deductions in the possession of the company at December 31, 2002. Supporting records and subsequent cash disbursements verified this item.

Payroll Taxes Payable **$50**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2002, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$317**

This liability represents the company's liability on expenses incurred prior to December 31, 2002, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accrued Vacation Pay **$1,690**

This liability represents the company's liability for vacation pay owed on December 31, 2002, which had not yet been paid. Supporting records verified this item. The company had failed to make an accrual for this. It is recommended that the company accrue for vacation pay on all future annual statements.

Accrued Salaries **$430**

This liability represents the company's liability for salaries owed on December 31, 2002, which had not yet been paid. Subsequent payment of payroll in January verified this asset. The company had failed to make an accrual for this. It is recommended that the company accrue for salaries payable on all future annual statements.

V. CONCLUSION

The company has suffered underwriting losses over three of the past four years. In 2000, the company had storms hit three different areas which caused the bad results for that year. In 2001, one area was severely hit again. The current year resulted in a profit of $46,429. Policies in force have grown from 1,089 to 1,210 during the period under review. There were two adjustments made to surplus during this examination and they can be found under Accrued Vacation Pay and Accrued Salaries. Surplus of $228,457 is close to the minimum surplus required of $200,000. The examiners reclassified certain unearned premium to advanced premium and certain advanced premium for an amount which should have reduced deferred premiums. The company hired an adjuster/inspector in 2001 to assist in getting the company profitable. The examiners made eight recommendations and one suggestion which follow this section.

The company has a high expense ratio, and surplus has declined 45% from $418,660 at year end 1996 to $230,577 at year end 2002. The company pays its two key employees a full-time salary, and allows them to work on TMA Agency, Inc. business during work hours. The company also pays TMA Agency, Inc., the same commission rates as all other agents. This report contains a suggestion that the company reevaluate this practice in light of its financial condition.

The company has earned negative investment income in recent years, due to a combination of low interest rates, few invested assets that produce an investment return, and expenses allocated to investment income ($11,526 in 2002) that exceeded cash received from investments ($3,456 in 2002). On December 31, 2002, 41% of assets, or 93% of surplus, is invested in Wisconsin Reinsurance Corporation common stock, an investment that does not pay dividends.

Because of the high expense ratio, negative investment income and the company approaching the minimum surplus for a town mutual, the company should continue to investigate the possibility of merging with another town mutual insurer.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 16 - Corporate Records — It is again recommended that the company replace directors according to its articles of incorporation and by-laws.

2. Page 16 - Corporate Records — It is recommended that directors be required to attend meetings regularly and, if any director cannot fulfill the obligation of regularly serving on the board, the company should consider replacing the individual with a person who is able to attend meetings regularly.

3. Page 17 - Holding Company — It is again recommended that the company file with this office, agreements for transactions between affiliates pursuant to s. Ins 40.04 (2), Wis. Adm. Code.

4. Page 17 - Holding Company — It is again recommended that the company annually file holding company reports in accordance with s. Ins 40.03, Wis. Adm. Code.

5. Page 18 Holding Company — It is suggested that the company re-evaluate its practice of paying its two key employees a salary and also paying TMA Agency the same commission rate as its other agents, in light of the company's diminished surplus and high expense ratio.

6. Page 18 Holding Company — It is also recommended that the company file an updated business plan with this office 30 days after the adoption of this report.

7. Page 22 - Cash and Invested Cash — It is recommended that the company keep signature stamps in a secure place, such as the company safe.

8. Page 28 - Accrued Vacation Pay — It is recommended that the company accrue for vacation pay on all future annual statements.

9. Page 28 - Accrued Salaries — It is recommended that the company accrue for salaries payable on all future annual statements.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, DuWayne Kottwitz of the Office of the Commissioner of Insurance (OCI), State of Wisconsin, participated in the examination:

Respectfully submitted,

David A. Grinnell
Examiner-in-Charge